

STATE OF MAINE
PUBLIC UTILITIES COMMISSION

Docket No. 2001-81

February 6, 2001

MAINE PUBLIC UTILITIES COMMISSION
Inquiry into Implementing a State Universal
Service Fund for Local Exchange Carriers

NOTICE OF INQUIRY

WELCH, Chairman; NUGENT and DIAMOND, Commissioners

I. SUMMARY & INTRODUCTION

This Notice of Inquiry (NOI) outlines a proposal for a State Universal Service Fund (USF), pursuant to the provisions of 35-A M.R.S.A. §7104. The USF mechanism proposed here is intended to allow eligible local exchange carriers (LECs) who are unable otherwise to meet their allowed intrastate revenue requirement to draw support from the Fund. The Commission seeks comments from any interested persons concerning the proposal.

The Commission began the development of a USF with a NOI issued on July 17, 1997, in Docket No. 97-429 and continued it with an NOI issued on October 27, 1998, in Docket Number 98-807. In each of those proceedings, the Commission set forth a proposed process for addressing USF issues and sought comments on a series of specific questions related to implementing one or more types of USF mechanisms. In each case, the Commission received comments from interested persons but never proceeded beyond that stage. The Commission has already incorporated the comments received in Docket 97-429 into Docket 98-807. We will further incorporate all of the comments received in either of those previous dockets into the current proceeding¹ (and possibly other USF proceedings, as appropriate). This proceeding will specifically address a USF support mechanism for rural LECs who, due to a combination of high costs and a loss of intrastate access revenue caused by 35-A M.R.S.A. § 7101-B, cannot achieve their overall revenue requirement and still maintain their local exchange rates at levels deemed affordable and comparable to those available in urban areas. We will refer to the support mechanism in this proceeding as the "High Cost USF", because it is designed to assist LECs that serve high cost areas.

The Commission's USF process also will move forward on a second, distinct track. In a separate proceeding, we will describe and seek comment on several options for a proposed system, to be known as the Fair Competition USF, whose purposes are to identify and make explicit any implicit subsidies contained in current rates and to establish a system to provide an amount of portable support that will encourage the development of economic competition for local service in all exchanges of Verizon

¹ We also close Docket No. 98-807 at this time.

Maine's service territory. Initially, we will limit the application of the Fair Competition USF to Verizon Maine's territory, because each of the independent ILECs still maintains the rural exemption pursuant to Section 251 (f) of the TelAct and, thus, will not experience local service competition until the Commission decides that the exemption should be lifted after considering a request from a CLEC. If and when we decide to implement the Fair Competition USF in the territories of the rural LECs, we will need to reconcile the operation of the High Cost USF with the Fair Competition USF, because the two mechanisms (as proposed) are based on different costing principles that may render them incompatible.

The main objective of the Fair Competition USF will be to promote economic competition everywhere in the State, regardless of whether the incumbent LEC is Verizon Maine or any of the independent telephone companies. This mechanism will be designed to minimize the opportunity for CLECs to engage in the practice known as "cream skimming," whereby they market only to high-usage customers in low-cost service areas. We want to encourage the development of local competition for all customers in Maine. Initially, however, we will deploy two separate USF systems to meet the needs of ratepayers in the various service territories.

The intent of the High Cost USF proceeding is to put in place a Commission rule that will be effective by the date of the next required adjustments to intrastate access rates, pursuant to § 7101-B, on May 30, 2001. Thus, the rule will allow any rural ILEC that we find to need high cost support to begin participating in the USF mechanism simultaneously with its required reduction in access rates. The Fair Competition USF is expected to require somewhat more time to complete, because the theories and mechanisms behind it are not yet fully developed. Nevertheless, because it represents a vital element in encouraging ubiquitous local service competition in Maine, our goal is to finish the Fair Competition USF proceeding as expeditiously as possible, with a current target date of December 31, 2001.

II. BACKGROUND

The High Cost USF is intended to accommodate policy objectives contained in state and federal statutes, some of which may conflict with one another. Title 35-A M.R.S.A. § 7101 sets forth certain telecommunications policy objectives for the State of Maine. Specifically, telecommunications policy must promote and encourage universal service, economic development and access to information services for all citizens of Maine. Section 7101-B of Title 35-A requires that intrastate access rates be adjusted periodically to a level that is less than or equal to interstate rates. Section 7104 further requires, among other things, the Commission to ensure that similar telecommunications services are available to consumers throughout the State at reasonably comparable rates. Section 7104 also sets forth the parameters and requirements that the Commission must follow should it decide to implement a state USF. Finally, § 7303 prohibits mandatory local measured service and mandates that the Commission establish traditional flat rates for local telephone service at as low a cost as possible.

At the federal level, the main goals of the TelAct are to promote local service competition, and simultaneously encourage affordable and comparable rates. Section 254 of the TelAct specifically establishes the national principles for universal service and for the establishment of a USF support mechanism, whose main purpose is to provide support for high cost service areas. Among its provisions is one requiring that customers in all areas of the country have access to telecommunications and information services, including interexchange services and advanced telecommunications and information services, that are reasonably comparable in function and quality and are available at reasonably comparable rates.

We were required, pursuant to 35-A M.R.S.A. § 7101-B, to set intrastate access rates at levels that were less than or equal to interstate rates on May 30, 1999, and we are required to re-set the intrastate rates on the same basis every two years thereafter. For the rural telephone companies, we issued an Interim Order on January 28, 1999, that required the independent ILECs to file tariffs for effect on May 30, 1999 reducing their intrastate access rates to levels that were equivalent to the levels of their interstate disbursements. Disbursements are the amounts that the companies receive from the National Exchange Carrier Association (NECA) access pool and are based on each company's actual separated interstate cost of service, as defined in FCC Rules at Part 36. We found that equating intrastate access rates to interstate disbursement levels was a reasonable basis for setting intrastate access rates, because each company had, and still has, the option of leaving the interstate access pool and filing its own interstate access tariffs, which would be calculated on the basis of the company's separated interstate costs. We found that this arrangement complied with the provisions of Section 7101-B, but we also ordered the companies to participate in a process that would reduce their intrastate access rates to the level of the NECA interstate tariff rates by May 30, 2001, the next date at which, according to Maine statute, intrastate access rates must be set less than or equal to interstate rates.

Each of the independent companies filed its required access rate reductions for effect on May 30, 1999, and then entered into discussions with the Commission Staff, the OPA and other interested parties. Based on an analysis of each company's then-current earnings position and the effect that reducing intrastate access rates to the NECA tariff level would have on the company's earnings, all the companies filed, and the Commission approved, stipulations which provided, in part, that all the independent companies would reduce their intrastate access rates to the NECA 5 tariff level on May 30, 2001. In response to the access rate reductions, nine companies agreed to file rate cases on August 30, 2000, while the others, except for two companies that had recently been sold and had individual stay-out provisions under the terms of the approval of their sales, agreed to two-way stay-outs until certain dates beyond May 30, 2001. The stay-out provisions prevented each company from filing a general rate case proceeding under Section 307, and also prevented the Commission, or any other party to the stipulation, from initiating a general rate cases proceeding under Section 1302. The purpose of the stay-out provisions was to recognize the possible existence of excess earnings during the period prior to the date of the access rate reductions, to be followed

by a commensurate period of potential under-earnings during the term of the stay out. At the end of the each stay-out, each company is permitted to file a rate case based on its then-current earnings position.

On August 30, 2000, Unitel, Community Service, Mid-Maine and the six Maine TDS telephone companies filed rate cases in accordance with the terms of their access rate stipulations. The rate cases currently in progress will produce an overall revenue requirement for each company, based on a reasonable rate of return, and a rate design will be adopted that will allow each company the opportunity to earn its allowed return. One possible rate design solution under consideration in these cases involves an increase in the basic exchange rates of each company. To adhere to the rate comparability requirements contained in state and federal law, we anticipate that the local rates of each company will not increase above the local rates of Verizon Maine for similarly-sized exchanges. That amount of rate increase, to approach or equal Verizon's rates, may be substantial for customers in some exchanges, and some type of phase-in may be needed to avoid "rate shock." Even with the potential substantial amount of local rate increase, some, and perhaps all, of the companies may not have sufficient revenues to allow them to earn a reasonable return. For that reason, we are proposing a High Cost Universal Service Fund that will provide additional support to companies that are found to be unable otherwise to have the opportunity to earn a reasonable rate of return.

III. FUND STRUCTURE

In this section, we will describe our proposal for the structure and mechanics of the State High Cost USF. Initially, we will discuss the process by which ILECs will be found eligible to receive support from the USF, and how the amount of support will be determined. We will then describe our proposal for determining how contributions into the fund will be made and who will make them.

A. Recipients and Amounts

In order to be eligible to receive high cost USF support, an ILEC will be required to undergo a rate case proceeding, pursuant to Title 35-A Section 307. The rate case will establish the company's intrastate revenue requirement, based on an examination and analysis of the company's costs (net of federal USF support amounts), rate base and a reasonable return on rate base. During the rate design phase of each case, the Commission will determine a reasonable level for the company's basic service and ancillary local rates, based on the affordability and comparability standards contained in Maine and federal law. One of the major criteria for deciding if the comparability standard is met will be to compare the independent company's basic service rates to those of Verizon Maine for similarly-sized exchanges and to allow increases up to that level.

We must rely mainly on subjective measurement criteria to assess the affordability standard in the statutes. The only metric, of which we are currently aware, that provides some indication of affordability is the percentage of households that have telephone service. Currently, the FCC calculates the penetration ratio on a statewide basis, and Maine leads the nation in that category. It is possible, however, that some companies, or certain exchanges within those companies, might have circumstances that would cause their penetration rates to be significantly below the statewide average, thus indicating that their local rates were not meeting the affordability standard. In those situations, we might want to implement measures, such as limiting the local rate increase and, instead, providing additional assistance from the High Cost USF that would help to improve the penetration rate. This issue may require further analysis and development, either in individual rate case proceedings or through a Commission investigation.

At the rate design phase of the rate cases, intrastate access rates will be set equal to the then-current NECA interstate rates, and local rates will be raised to levels approaching or equal to those of Verizon Maine for similarly-sized exchanges. If, after those adjustments, a company is found to be unable to meet its allowed revenue requirement, any remaining deficiency will be recovered from the High Cost USF. Based on the company's annual revenue shortfall, the company will receive equal pro rata monthly payments from the USF. The company will continue to receive the monthly USF amount until the Commission orders a change or a cessation (by rule or order), or until the company voluntarily decides that it no longer needs the payment. Because Maine law requires that intrastate access rates be adjusted every two years, and because changes in the basic structure of interstate access rates are expected to be implemented in the near future, our Rule will be flexible enough to accommodate any changes in payment level that are needed. The Rule will likely include a provision allowing the Commission to waive the requirement that a full rate case proceeding be conducted prior to any change in the amount of High Cost fund support payments, if the Commission finds that an adjustment to the USF payment amount is warranted. A change in payment amount may be caused by extraneous or exogenous events or factors, or a change in competitive or regulatory factors. The waiver and subsequent change in payment amount may occur on an individual company or a broader basis.

B. Contributions to the Fund

We next turn to the method by which the funds needed to provide the High Cost USF support and to provide compensation for a fund administrator will be collected. Because the need for the support is driven in large part by the mandated changes to intrastate access rates, we plan to collect the needed fund amounts through an assessment on the intrastate revenues of all interexchange carriers (IXCs), paging

companies and wireless carriers, as permitted under Section 7104.² The revenues that will be used as the basis for determining the individual IXC contributions to the High Cost USF will be the annual intralata interexchange revenues reported by the IXCs in their most recent Annual Reports filed with the MPUC and the revenues reported to the Commission by the paging companies and wireless carriers for use in assessing contributions to the Telecommunications Equipment Fund, pursuant to 26 M.R.S.A. § 1419-A. While we recognize that actual ongoing revenues will vary by company, fixing the base on which the carriers pay will bring a measure of stability to the calculation of contribution amounts. The fund administrator will establish on a forward-looking basis the percentage of each carrier's reported revenues that must be paid into the High Cost USF. The administrator will know, based on the Commission's decisions regarding individual LEC eligibility for payments from the fund, the amount of money that must be disbursed from the fund. To this the administrator will add the cost of administering the fund, and this total will be the numerator in the fund calculation formula. The administrator will also know the revenue base on which contributions from the carriers will be based. This is the denominator in the formula. Determining the contribution of each carrier will involve multiplying the percentage result from the fund formula by each carrier's annual revenue amount.

The administrator may bill the carriers on a monthly, quarterly or semi-annually, depending on its preference after consultation with the affected carriers. The administrator will consider the likelihood that the payment amounts will remain steady over the period in question, the administrative burden (on its part, on the part of the carriers paying into the fund, and on the ILECs receiving payments from the fund), and the cash flow implications of its receipt and payment cycle. The administrator will recalculate the fund payment percentage whenever it determines that a change in the amount of payments from the fund will occur. This process should be relatively straightforward, because changes in the amounts of the payments from the fund can only occur with an express written order of the Commission.

IV. CONCLUSION

The Commission seeks comments from interested parties of all aspects of the High Cost USF proposal presented here. Interested parties may comment about the theory underlying the mechanism and about the specifics of the proposed plan. We are including no specific questions in the NOI, but invite written comments on any aspect of the proposal.

Written comments should be submitted by February 27, 2001, and depending on the scope of the comments, a technical conference may be convened to allow the Commission and interested parties to discuss the proposal and the filed comments

² We have already established a Telecommunications Education Access Fund (MTEAF), pursuant to 35-A M.R.S.A §7104-B and Chapter 285 of our rules. These same carriers will be accessed up to .5 % of retail charges beginning July 1, 2001 for the MTEAF.

interactively. The Commission then intends to open a rulemaking that will produce a final rule establishing a High Cost USF by May 30, 2001.

Dated at Augusta, Maine, this 6th day of February, 2001.

BY ORDER OF THE COMMISSION

Dennis L. Keschl
Administrative Director

COMMISSIONERS VOTING FOR: Welch
 Nugent
 Diamond

NOTICE OF RIGHTS TO REVIEW OR APPEAL

5 M.R.S.A. § 9061 requires the Public Utilities Commission to give each party to an adjudicatory proceeding written notice of the party's rights to review or appeal of its decision made at the conclusion of the adjudicatory proceeding. The methods of review or appeal of PUC decisions at the conclusion of an adjudicatory proceeding are as follows:

1. Reconsideration of the Commission's Order may be requested under Section 1004 of the Commission's Rules of Practice and Procedure (65-407 C.M.R.110) within 20 days of the date of the Order by filing a petition with the Commission stating the grounds upon which reconsideration is sought.
2. Appeal of a final decision of the Commission may be taken to the Law Court by filing, within 30 days of the date of the Order, a Notice of Appeal with the Administrative Director of the Commission, pursuant to 35-A M.R.S.A. § 1320(1)-(4) and the Maine Rules of Civil Procedure, Rule 73, et seq.
3. Additional court review of constitutional issues or issues involving the justness or reasonableness of rates may be had by the filing of an appeal with the Law Court, pursuant to 35-A M.R.S.A. § 1320(5).

Note: The attachment of this Notice to a document does not indicate the Commission's view that the particular document may be subject to review or appeal. Similarly, the failure of the Commission to attach a copy of this Notice to a document does not indicate the Commission's view that the document is not subject to review or appeal.